

**Discretionary policy-making in the Commission:
the politics of EU state aid control**

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Introduction

It is not unusual to come across articles on European competition policy which argue for the exclusion of politics from the competition policy process. Even the EU's state aid regime, which involves perhaps the most political of all the European policies, has been subject to such calls (Bishop, 1997: 84). These aspirations of a 'politics-free' or perhaps more realistically, of a 'depoliticised' type of enforcement deserve further attention. After all, the very notion of a depoliticised state aid regime is likely to be deemed a contradiction-in-terms by many commentators (this author included).

The premise upon which this paper is based is that the political input into state aid control is not only the preserve of the College of Commissioners in controversial and well-publicised high-profile aid cases, but occurs (directly and indirectly via the medium of discretion) at many stages and in different ways within the Commission's state aid regime. It occurs directly through the many 'instances of discretion' that exist during the state aid decision-taking process; and it occurs indirectly, through the self-imposed restriction of that discretion; that is, in the formulation of policy, through codified guidelines and the use of principles which serve as criteria during the decision-taking process.

The importance of discretion and executive rule-making has long been recognised especially in the fields of welfare and criminal justice (Davis, 1974; Adler and Asquith, 1981). Discretion has been defined in many different ways, with the common denominator seeming to be an emphasis on choice and/or judgement within the policy process (Ham and Hill, 1984: 149). Indeed, it is this element of choice and

judgement which lies at the heart of this paper's definition of politics.¹ While the discourse on this topic usually revolves around the merits of flexible versus rule-bound decision-making, or arbitrariness versus legal certainty, the underlying presumption in many cases is that discretion is something to be discouraged, a negative aspect of the policy process. However, the resultant calls for a 'return to legality' (Adler and Asquith, 1981: 9) simplify the options open to policy-makers, as we shall see.

This paper explores the European Commission's capacity for supranational discretionary decision-taking through the lens of its state aid policy. It begins by introducing the state aid regime and by highlighting the inter-institutional autonomy of the Commission. It then charts the incidences of discretion that occur throughout the state aid decision-taking process, providing at the same time an introduction to the way in which such decisions are taken in this policy area. The paper then goes on to identify a separate Commission policy-making process, highlighting the Commission's use of guidelines which form the basis of its policy applied to individual decisions. The paper ends by addressing two sets of questions: on the interplay of discretion and criteria in the state aid regime on the one hand; and on the lessons to be learnt not just about state aid matters but also about the European Commission on the other?

The EU's state aid regime

The Commission's state aid policy has far-reaching implications. In restricting the freedom of manoeuvre of national and sub-national authorities to grant subsidies

¹ It has to be said that there are often misunderstandings the word 'politics' is often interpreted differently in different contexts. Th author's definition of politics is inclusive - add clear and broad definition!!

within parameters established in Brussels, it could be said that the policy sounds the death-knell of national interventionist industrial policy. However, despite the fact that the Treaty of Rome endowed the Commission with powerful legal tools which it could use to combat divisive and discriminatory governmental behaviour, it is only fairly recently that a coherent state aid policy has been developed. There is no doubt that the Single Market Programme had much to do with the ascendency of the policy at the end of the 1980s. Indeed, the importance of state aid control for the completion of the Single European Market (SEM) is beyond doubt. The case that the SEM would be jeopardised by unchecked state aid has become almost a truism, even though there are clearly other crucial impediments to the emergence of a fully unified European market. However, as physical, regulatory and fiscal barriers to trade are removed, the temptation to use subsidy as a way of compensating for inefficiencies must be overwhelming. Indeed, without an effective system of surveillance and control, state aid would remain as one of the few protectionist devices at the disposal of national and sub-national authorities. This argument is all the more salient in view of the impending Economic and Monetary Union (EMU) deadline, and the notion that a strict approach to state aid could contribute to states meeting the EMU convergence criteria.

The EU's state aid regime is governed by Articles 92-94 of the Treaty of Rome (amended slightly by the Treaty on European Union) (Appendix 2). Article 92(1) prohibits state aid and is somewhat of a catch-all provision, while Article 92(2) and 92(3) allow for derogations from the prohibitive rule, mandatory in the case of the former and discretionary in the case of the latter (Appendix 1).² Article 93 spells out

² Other exemptions include Article 42 (agriculture), Article 77 (needs of coordination of transport or reimbursement for discharge of obligations inherent to public service), Article 90(2) (undertakings entrusted with services of a general economic interest or having the character of a revenue producing monopoly), Article 223 (military industry) and Article 4 ECSC (coal and steel).

the state aid procedures: requiring the Commission keeps under review existing state aid; offering rights to third parties; allowing for judicial review; granting the Council the right unanimously to derogate from Article 92; and instituting a system of prior notification which suspends the grant of the aid in question. Finally, Article 94 allows for a Council regulation (so far unused) on the basis of a proposal from the Commission.³ The EU's state aid rules are administered by Directorate G in Directorate-General Four (DGIV) of the European Commission by about 100 staff, around 50 of which are 'A' grades (Appendix II). It is DGIV which is responsible for the operation of the EU's competition policy. But while most of the directorates within the DG deal with 'competition between firms' (that is, anti-trust policy), the state aid directorate concerns itself with 'competition between governments'.

Although the means are very different, the ultimate objectives of the two sides of the competition policy coin are the same: to contribute to the creation of a level-playing field for European industry and the creation of a fully unified single market in which both free and fair competition can flourish. However, as Faull (1994) has stated, '[t]he creation of a wholly level playing-field throughout the Community's territory is now seen by many, rightly or wrongly, as [a] misplaced and over-reaching ambition'. With the cohesion principle now firmly ensconced within the treaty framework, the case for a competition policy which does not always adopt the competition line finds itself on firmer ground. There has always been consideration of 'other' Community objectives when considering competition cases (whether anti-trust or state aid), this seems more appropriate now than ever before. As Evans and Martin (1991: 110) argue, 'state aid is increasingly seen as a vehicle for making the completion of the

³ There is Council legislation only in the fields of agriculture, fisheries, transport, coal, steel and shipbuilding.

internal market politically acceptable'. Over the 1980s, the rhetoric of neo-liberalism allowed the DGIV staff to shout louder than many others within the Commission, and many (at least in the state aid case) were foolish enough to believe that rhetoric. The reality was somewhat different, with regional, social, environmental and perhaps most importantly of all, pro-competitive industrial policy objectives also taken into consideration throughout this period. This is not to say that DGIV was an agency of interventionism masquerading as an advocate of deregulation - far from it - but it is clear that the purist impression of the European competition regime does not always equate with the decisions that were taken over the course of the 1980s.

While the supposed neo-liberal credentials of the state aid directorate are challenged here, its supranational characteristics are beyond doubt. Indeed, here is a part of the Commission whose competence must remain untouched by the decentralising impetus of subsidiarity. In fact, as a centralising as well as a decentralising force, the subsidiarity principle only serves to strengthen the Commission's role in this policy area. However, while member governments generally accept this (the new UK Labour Government even mentioned the need for tighter control of state aid in their election manifesto), individual cases can be highly contentious. Traditionally, national and regional governments have determined the industrial rules of the game, and as such, have altered and redirected the competitiveness of particular sectors in particular regions for economic, political and social motives. 'Competitive subsidisation' is just one way in which they have been able to achieve this. However, subsidisation is pointless if its objectives fail to be achieved. Subsidies granted by one government are often countered by subsidies in competitor states. Such subsidy battles invariably lead to a very high overall level of state aid, aid

which in the final analysis has little if any impact on competitiveness. To prevent the emergence of this sort of costly 'subsidy trap' the Commission steps in.

In restricting a government's room for manoeuvre, the scope for competition between (member state) governments is curtailed. State aid may still be granted, but only within the quantitative and qualitative limits established by DGIV. As such, it is now DGIV which establishes the rules of the game - at the European level and for the benefits of European industry. However, governments that tend to assess industrial, regional and social problems from a national or a local rather than from a European stand-point are unlikely to see Commission involvement in this light.

Inter-institutional autonomy and inter-institutional constraints

The Council and the Parliament

The inter-institutional relationships that underpin the enforcement of state aid policy are very different from those that characterise other EU policies. The Commission (as is often said of it in anti-trust cases) acts as prosecutor, judge and jury in individual cases, whilst at the same time being responsible for the evolution and substance of the broader policy on state aid. This EU policy is, to be more precise, a Commission policy, as the uniqueness of the regime lies in the Commission's independence from both the Council of Ministers and the European Parliament. Only where there is a direct Council intervention in an aid case under Article 93(2) (a rarity) or when an Article 94 Regulation is proposed (so far never realised) is there formal Council involvement in the decision-making and policy-making processes. It is clear then that the Council plays the junior role in the Commission-Council relationship which implies

that the Commission is able to act on state aid matters relatively free from formal member state constraints. This places the Commission in an unusual position.

Despite this relative freedom, the Commission has been active in granting concessions to the Council. These have taken the form of increased access to information on state aid cases; the discussion of the Commission's annual competition reports in the Industry Council; and the setting up of formal multilateral meetings of member state experts (Commission, 1990). In the case of the latter, frequent and fairly informal meetings have helped to prepare the ground for new policy developments, although this has not entirely done away with legal challenges to Commission guidelines. However, moves to involve the member states in discussions over both specific aid cases and broader policy and procedural change should not be judged to involve any transfer of control or surveillance over state aid matters. Indeed, such changes can easily be interpreted as a rearguard action by the Commission to undermine those governments pushing for more Council oversight of state aids matters..

Even though the DGIV staff are legally entitled to tell national governments how *not* to spend their tax revenues, this does not mean that it is in the Commission's interest to be heavy-handed in its enforcement of the state aid rules. Indeed DGIV may shrink from taking action in a controversial case, even when it is well within its legal capacity, as 'the Commission is not always politically in a position to act in those areas in which it has the legal right' (Warnecke, 1978: 170). At times this may be the result of internal constraints placed upon the directorate by the College of Commissioners, but it may also on occasions be a reaction to wider threats to the inter-institutional position of the Commission within the EU. Commission officials would be foolish to

aggravate national governments to the extent that this might lead to calls for a reduction in the Commission's formal powers. DGIV would prefer to be seen to be acting with tact and reason and even, at times, with self-restraint.

Commission officials are keen therefore to keep their relationship with the member states on friendly terms. The bilateral relations between the state aid directorate and the Permanent Representations makes this possible. It is not unusual for national representatives to meet regularly with state aid staff to discuss a particular case. This helps to keep the two-way information flow in tact. The bilateral relationship between DGIV and national representatives tends to work against the latter however, allowing DGIV a monopoly of information as well as the right to propose the final decision. DGIV alone has the overview necessary to understand the workings of its own policy, although recent clarifications of the rules (since 1989) have helped to improve this situation. In the past, the Council's position was undermined as its exclusion from multilateral forums placed limits on its knowledge of the policy. However one should make the distinction between general policy discussions that can now take place in the Council and between Commission and member states multilaterally on the one hand, and bilateral contacts that tend to prevail where individual instances of state aid are at issue. A purely bilateral set of relationships is clearly not sufficient to provide for an overall EU strategy towards state aid (Urciuol, 1990: 651). The agreement that competition policy should be discussed in the Council from 1989 and the presence of the Commissioner or his representative at the Industry Council, has helped to keep the member states better informed.

It is possible that the relationship between Commission and Council will change to an even greater extent in the next few years as an Article 94 regulation proposed by

the Commission, to be agreed by the European Parliament and the Council is on the state aid agenda. This is something of a u-turn on the part of the Commission, given that until very recently DGIV has been firmly opposed to such a move.⁴ However, in view of the resource constraints and the ever-increasing workload facing the DG this should perhaps come as less of a surprise (Stuart, 1996: 226). The proposal for a regulation, that is, for implementing legislation, is in any case likely to be based on the accumulated experience of the state aid directorate, and it would not be unreasonable to imagine that the outcome will be little more than the formalisation of current Commission practice. Whether such a proposal would face opposition in the Council is another matter of course. At this stage we can do little more than speculate.

The European Parliament is also at arm's length from the enforcement of state aid, although it does receive information on aid matters and is able to comment formally on the Commission's annual competition reports. It would also be consulted on any proposal for an Article 94 Regulation (a change introduced in the Treaty on European Union). Even so, for both institutions what we are witnessing is something far less than direct policy involvement. Both the Council and the Parliament are not without their influence however, as taking heed of Council/EP concerns is a way of tempering later complaints about the non-accountability of the officials running the policy and of limiting calls for the restrictions on the Commission's powers. This may be more a damage-limitation exercise than a real consideration for inter-institutional co-operation, but the end result is the same.

⁴ Regulations were proposed in 1966 and 1972, but these failed to lead to agreement in the Council and were both subsequently withdrawn. See Mederer (1997). Ehlermann (1995) has said that the Council cannot deal rationally with state aid matters and that horse-trading and hostage-taking will always characterise their state aid dealings.

The Court

The onus on case-law (resting on the framework of the state aid treaty provisions) to provide the only formal foundation for an EU state aid policy has made the European Court's line on state aid a key determinant of both substantive and procedural policy. As DGIV's quasi-judicial procedure allows for the direct referral of cases to the Court (Wyatt and Dashwood, 1980: 333) it could even be argued that the Commission-Court relationship has taken the place of the more conventional Commission-Council one (Goyder, 1988: 375).

Until the early 1980s, the Court's role was consistently supportive of the Commission's approach to state aid enforcement. This is perhaps surprising given the ineffectiveness of the state aid rules at that time. There was certainly a danger at the time that should the Court come to be considered as nothing more than an extension of the Commission, consistently confirming in law the line taken by the Commission, the perceived loss of impartiality would certainly be detrimental to the reputation and standing of both institutions, but in particular to the Court. As a certain detachment or objectivity is central to the functioning of any court, the door would then be opened to fairness and justice becoming little more than instruments of Commission policy. Such a scenario is not as extreme as it might at first appear given the inherent goal-orientated teleological approach of the Court in its role of interpreter of the treaties (Rasmussen, 1990). Therefore, increasing criticism by the Court of the Commission's state aid decisions in the early 1980s was welcomed as evidence of its objectivity and fairness. The change took place in the form of more intolerance of procedural inadequacies in the Commission's submissions (inadequate reasoning was often cited) and a willingness to dismiss cases on such grounds. The fact that more cases than ever

are going on appeal to the Court seems to suggest a growing confidence of the European legal order in the member states. It also had the consequence of improving the standard of the Commission's reasoning in its decisions (Schina, 1987: 154).

While the Court does act as an institutional constraint on DGIV, the negative impact of this should not be exaggerated (Ross, 1989: 894). The supportive role of the Court is now only rarely negated by procedural errors on the part of the Commission; and the Court rarely criticises the substantive reasoning of the Commission as long as the process of its reasoning is adequate. As Evans and Martin (1991: 89) agree, '[p]rovided an explanation is given, the substance of the analysis cannot easily be challenged'. With fewer challenges to the substantive argument of the Commission, the Court increasingly rests its cases on procedural foundations alone.

Again, things may be changing for the Commission-Court relationship. Part of this is simply due to the fact that the state aid case law has been growing, which itself acts as a constraint upon the Commission's freedom of manoeuvre. Most certainly, the establishment of the Court of First Instance in 1989 and, since 1993, its function as first port-of-call for state aid appeals made by natural or legal persons (ie firms, rather than governments) seems to mark the beginnings of what may ultimately be a sea-change. The increasing number of cases brought by firms is itself an interesting trend, marking a growing awareness of the state aid rules and a recognition that the Commission policy of demanding the recovery of aid would possibly damage the firms more than the grant-giving authorities. Although it is perhaps too early to make sweeping generalisations about the impact of the CFI on Commission reasoning in state aid cases, it is clear that the CFI has been less cautious in its unpacking of the Commission's argumentation and has been keen to examine the factual basis of its

reasoning (Hancher et al., 1993: 15). This may well send signals to the Commission that its decisions must become more explicit in future.

State aid decision-taking and instances of discretion

Discretionary decision-making in the state aid field is extensive, characterised by a procedural and substantive freedom which is unique. This section of the paper charts the Commission state aid decision-making process and identifies the points at which discretion is applied within that process.⁵

The state aid rules oblige the member states to inform the Commission of the grant of any new or altered state aid.⁶ It is this system of notification which forms the basis of the Commission's state aid regime. In practice, however, it is extremely problematic as it relies upon the national authorities to submit voluntarily to the scrutiny of the state aid directorate. Not surprisingly, avoidance and non-notification are wide-spread (113 identified in 1995). The Commission has variety of ways of uncovering unnotified aid however: it is especially reliant on complaints made by competitor firms and states, and on information gleaned from the financial or trade press. But as non-notified aids are not in themselves 'illegal', it is often in a member state's interest *not* to notify them to the Commission, especially when they are unlikely to be granted.

The preliminary investigation

⁵ Hancher (1994: 134) lists three areas of discretion: the determination of whether a particular measure involves an element of state aid; the decision as to whether any of the main categories of exemptions apply to the state aid; and the progression of the state aid inquiry.

⁶ There were 680 new notifications in 1995.

The preliminary stage of state aid decision-taking is often depicted as being rather routine. As we shall see, this is far from an accurate portrayal of this step in the enforcement process.

Once a notification has been received and acknowledged by the Commission, the first question the *rapporteur* in charge of the case must ask is whether the measure is in fact a *state aid* under the terms of the Treaty. Usually it is, as the definition of an aid is broad enough to cover almost all governmental assistance, to the extent that Article 92(1) verges on a *per se* rule (Evans and Martin, 1991: 87). There are however a number of tests that state aid officials can do at this stage, as well as a number of conditions that need to be fulfilled (Quigley, 1993: 28), namely: is the measure granted through state resources?; does it distort or threaten to distort competition by favouring certain undertakings or the production of certain goods?; and does it affect trade between the member states? It is clear now that an aid must provide the firm with an economic advantage it would otherwise not have; that it excludes general measures; and that it must affect interstate trade perceptibly (Commission, 1996: pnt 156-62). While in the majority of cases these questions lead the *rapporteur* to a clear-cut conclusion, there a number of grey areas that remain problematic for the Commission, such as those involving the relationship between the member states and public sector firms (Hancher, 1994). It is often in these grey areas that the Commission's discretion is most visible.

The principle used to assist the Commission in its decision-taking in this area is known as the market investor principle (or the private commercial investor principle). It is used both as a means of identifying and quantifying aid (Bernitsas, 1993: 113-4). Only when the state is acting as a private investor is a measure (such as an injection of

capital) deemed *not* to be a state aid. In other words, when assistance is granted where a private investor would not invest, state aid is said to exist. The principle is contentious as definitions are contested: exactly what would a private investor invest in?; and should political, social or philanthropic considerations also be taken into consideration? It is clear that in the past this principle was something of a ‘blunt instrument’ of analysis (Abbamonte, 1996: 259). However, it seems that the Commission and the Court are now using it in a more sophisticated manner, taking into account the fact that a private holding company might act rather differently from a private investor and have motives other than short-term profit (Abbamonte, 1996: 259).

Decision-taking at this stage in the procedure is highly centralised and insulated within the Commission. As such, it is not surprising (or indeed inaccurate) that we should talk about state aid *control*, rather than state aid surveillance. The judgement made is effects-based and has been clarified by the Court on numerous occasions (as in the *Matra* judgement).⁷ What is also clear from these Court judgements is that the Commission has scope for discretion at this point in the decision-making process, even if most of the decisions taken are routine. Even so, the Court does want to see the Commission being more explicit in its use of market evidence. This does not imply any need for a quantitative approach to analysis, but it does suggest the need for some sort of geographical and product market assessment (Kobia, 1996).

The second question asked at this stage, assuming that a state aid is deemed to exist, is whether the aid is likely to fall under any of the Article 92 exemption clauses (appendix 2). This question is applied in a fairly informal manner. Where any doubt

⁷ Case C-225/91R *Matra v Commission* [1991] ECR I-5823; OJ 1992 C182/8; OJ 1993 L20/14.

exists the aid should not be approved. The state aid officials are so used to dealing with routine cases at this stage that an initial reading of the notification is often enough to allow firm conclusions to be drawn about its compatibility. There is no need for a step-by-step analysis undertaken in any formal sense. It should not be forgotten that the majority of work done by the state aid directorate is in effect the rubber-stamping of clear-cut notifications that do not in any way infringe the treaty provisions. We should not be surprised that this routine decision-making does not get the attention it deserves as routine cases are never as exciting as the more infrequent yet more high-profile state aid controversies. There are of course the grey areas where the compatibility of the aid is a matter for debate. But even here the decision to allow an aid, or to open the full investigative procedure under Article 93(2) is more to do with the gut-feelings of the *rapporteur* than with any specific and detailed economic or legal analysis (Evans and Martin, 1991: 83-6).

This is not to imply that the decision is arbitrary (Kobia, 1996). The state aid staff has a great deal of experience in dealing with such cases and there is always the threat of a Court appeal hanging over the Commission. If there is any concern about the effects of a measure there must be a full investigation. The *preliminary* investigation is intended to be just that - preliminary and impressionistic. There are so many cases to deal with at this stage that it would be impossible for it to be otherwise. There is, even so, an inherent ambivalence about the state aid procedures at this early stage. With state aid defined so broadly, and the number of notifications required by the Commission so large, the officials seek to dispose of the routine-type notifications as quickly as possible so as to concentrate on the most important cases. The

preliminary investigation performs a function bureaucratically that a more selective procedural framework would do legally.

The majority of notified cases will be authorised by a letter sent to the member states at the end of the preliminary period. Time limits are a source of serious contention at this stage and indeed they remain so throughout the entire procedure. Also increasingly contentious is the position of competitor firms (and third parties) who generally have little if any input during the preliminary stage. As they have no entitlement to information on the preliminary investigation, their only option is to take the Commission to the Court (now the CFI) once a positive decision (approving an aid) had entered the public domain (Commission, 1987: 310). At the moment they can only do this if they can demonstrate that they have a direct and individual concern in the aid. In the interests of speedy decision-making the rights of all competitors are limited. This is frequently challenged by state aid lawyers and adds to the criticism that the state aid directorate is making and altering its policy on an *ad hoc* basis without due regard to the effect that impromptu policy changes must have on the business community.

Albeit informal in its own right, the preliminary investigation is only one facet of state aid decision-taking. Frequently, a more informal 'procedure' is in operation, with member states informing DGIV directly of the existence of a measure which they believe either *not* to be an aid, or which they claim is clearly exemptible. As this aid has not been formally notified, it does not at this point enter formal decision-making channels. Of course, some of the aid which comes to the Commission's attention in this way will ultimately be challenged by DGIV and will have to be formally notified. The aim of member state authorities in seeking an informal reaction to a measure is simply

to receive the 'word' of the state aid directorate in the form of a comfort letter, a (non-binding) statement that no further action will be taken. This approach has been used by the Commission as a way of cutting down on DGIV's workload and is particularly useful where cases are routine. It satisfies the member states as matters are usually dealt with more speedily than under the formal procedure. Likewise, the state aid directorate is satisfied, as it has more time to spend on the more damaging aid. It is very likely that there are cases of a potentially more controversial nature that member states have sought to slip through the net using this approach. The state aid officials are unlikely to be fooled however. They see informality more as for their own convenience than for that of the member states.

So, although this stage in the decision-making process may be considered by some as routine and uncontroversial, there is evidence here, potentially at least, of both open and formal, and hidden and unaccountable instances of discretionary behaviour. These cases may not be documented and as such do not enter 'real world' of formal decision-taking. Interests are not involved and the public are not informed. Even during the more formal preliminary procedure, discretionary decisions must be taken: to define an aid; to decide on the content of the proposal (this may colour the reading of the case higher up the hierarchy); and to propose the initiation of the second stage in the state aid procedure. The preliminary state aids investigation is anything but routine.

The 'contentious' procedure

Once a preliminary investigation has taken place, the state aid directorate must decide whether there is a case to answer or whether doubts about the aid's compatibility with the treaty provisions still exist. If there are doubts, the formal proceedings under

Article 93(2) is initiated. This decision to investigate a case further is another instance of discretion in the state aid procedure although it relates directly to the assessment of an aid and its potential for exemption. It is clear that the Commission uses this discretion strategically. For example, it was stated in its *Twenty-Fifth Report* (1996: pnt. 209) that the contentious procedure had been opened in a number of internationalisation schemes '[t]o establish a clear policy in this field'. The opening of the Article 93(2) procedure means that decision-making enters the public domain, and this in turn implies that a statement is being made about the importance of the case - whether in political, legal or economic terms. With limited resources the state aid directorate does not have the capacity to pursue all state aid cases through to final decision. Increasingly it has come to recognise the importance of prioritising its formal investigations.⁸ In the *Twenty-Fourth Report* (1995: pnt. 395), for example, it was stated that 'the Commission can devote only limited staff numbers and resources to its departments dealing with state aid. It therefore has to concentrate on priority work and allocate resources accordingly'. Legally, it is important that the Commission's decision at this point in the proceedings can be reversed by the Court on appeal (Hancher, 1994: 143). This is particularly important for third parties who wish to challenge the Commission's tolerant treatment of an aid measure. Without the opening of a procedure, competitors have no rights at all.

This second stage in the decision-taking process involves a much more in-depth appraisal of the aid (albeit without any ground-level powers of investigation), in line with the criteria laid out in the treaty and in subsequent case-law and guidelines, and in consultation with the member states. However, some commentators still see the

⁸- Note that in 1995, 506 cases raised no objection and in 57 cases the Article 93(2) procedure was initiated.

economic analysis at this stage as inherently weak, especially when compared to the Article 85 and 86 market analysis (Bishop, 1997). The fact that the Court has not been particularly tough on the Commission in this respect allows directorate officials a greater scope for the discretionary decision-making that in any case goes hand-in-hand with the state aid exemption rules in Article 92(3) (appendix 2). Discretion at this stage has been confirmed in numerous court judgements and involves the weighing up of the pros and cons of the aid in question. In taking a decision based on Article 92, the Commission has the capacity to inject economic, social and regional considerations into its decision-taking in recognition of the advantages to be had from state aid and alongside an acknowledgement of the importance of the Community context. As Wishlade (1993: 143) has said with regard to regional aid, 'the notion of competition as an instrument of economic and social cohesion has become a standard defence of (often controversial) decisions on state aid'. State aid can clearly serve a multitude of policy goals, whether directly or indirectly, correcting market imperfections especially where externalities exist. In Article 92(3), the fact that the exemptions listed 'may' be compatible with the common market is crucial, as this is what gives the Commission its treaty-based flexibility.

The 'compensatory justification' principle forms the basis of the Commission's decision-taking when applying its discretion under Article 92(3). It has been used consistently in Commission decisions since it was confirmed by the European Court in the *Philip Morris (Holland)* judgement of 1980,⁹ although in practice it has underpinned Commission thinking since the 1960s (Mortelmans, 1984). The approach was initially spelt out in the Commission's *First Report on Competition Policy* in 1972

⁹ Case 730/79, *Philip Morris* [1980] ECR 2687.

where it was stated that the Commission was aiming to 'enable the Community authorities to act in a basically realistic manner in their control over aid, and to authorize actions which will contribute to the attainment of the general objective laid down in Article 2 of the Treaty' (Commission, 1972: 112-3).

This was the pragmatic common sense approach that has shaped the policy from the outset. Perhaps the clearest statement of the principle itself came however in the *Tenth Report on Competition Policy*, where it was stated that:

...if the Commission has to use its discretionary power not to raise objections to an aid proposal, it must contain a compensatory justification which takes the form of a contribution by the beneficiary of aid over and above the effects of the normal play of market forces to the achievement of Community objectives as contained in the derogations of Article 92(3)EEC (Commission, 1981: pnt 213).

It is clear therefore that the regulation of state aid allows for the balancing of the effects of legal certainty against a more flexible approach. The compensatory justification analysis opens the door to a qualitative cost-benefit analysis undertaken by the state aid staff, within which the losses to European competition are balanced against the gains in terms of other policy objectives and most notably in terms of industrial competitiveness and cohesion..

At this second stage in the proceedings third parties are not that much better informed than at the preliminary stage, although they do at least have certain rights. While the member states are kept informed of cases through their Permanent Representations, competitors often find it difficult to get hold of information at an early stage. A rather sketchy summary is published in the Official Journal, though this

does not give too much away. The Commission is extremely cautious about publishing information which could affect share prices. This leaves most competitors having to seek redress through the courts as a last resort. Thus, the final decision taken by the Commission has to be detailed and legal sound enough to enable it to stand up in the Court on appeal, though many would argue that this does not imply that the decision is in fact well-reasoned (Bishop, 1997: 85). A shoddy, speedily drafted and poorly investigated decision will involve risks. On the other hand, the Court may penalise the Commission (by not allowing the recovery of the aid for example) if there is too great a delay in issuing a decision.

At the end of the second stage the Commission will issue either a positive, a negative or a conditional decision. Conditional decisions might include restrictions on the type, amounts, intention, beneficiaries, purposes and/or duration of the aid (Commission, 1994: 396). Before this can happen drafts of the proposal are passed up the directorate hierarchy and are often returned to the *rapporteur* for reworking. In all but the most routine cases, the staff in Directorate A of DGIV will also vet the proposal before it is passed on to the Commissioner's staff (the *cabinet*). Other Commission services also get the opportunity to view the proposal when it goes into interservice consultation. The draft is circulated to interested DGs (and will as a matter of course go to the Legal Service). If there are any serious problems an interservice meeting may be held to try to iron them out.

Just as it is accurate to say that the majority of notifications do not end in the opening of a procedure, likewise it used to be true to say that most procedures do not end in formal decisions (Pijnacker Hordijk, 1985). Things are changing however. In 1995, for example, there were 22 positive final decisions, 9 negative final decisions and 5

conditional final decisions. The number of procedures opened in the same year totalled 57. However, it is still common for more informal settlements to be reached involving either modifications to the aid proposal, or the complete withdrawal of the proposal if it is unlikely that the Commission will accept it. It has been said however that '[v]ery few grants of aid are approved by the Commission once it has decided to initiate the procedure in Article 92' (Cownie, 1986: 262). Member states are not unaware of this.

The decision to take a decision is an arcane but an important one. Indeed, it is perhaps the most crucial part of the decision-making process. Without formal decisions there would be no more case-law. While the informal procedure may well resolve the problem of the individual grant of aid, it does not make any contribution to the broader legal and policy framework. This policy-making objective necessitates the formality which is part-and-parcel of the contentious procedure and links the Commission's decision-making in individual cases to its policy-making function..

The 'even more contentious' stage

Although the draft proposal is drawn up by the staff of the state aid dimension, it is the College of Commissioners assisted by their personal staffs (their cabinets) who in all but the most routine cases take the final state aid decision. This leaves open the possibility that the last stage in the decision-making process will be subject to a process of political bargaining. Within the College there is scope for political discretion in the taking of state aid decisions, with the proviso that the decision must stand up on appeal in the Court. But it is clear that the College may be able to profit from the Court's defence of Commission discretion earlier in the decision-taking process to unpick a proposal put before it. As Bishop (1997: 84) states, it is the *ad hoc* reasoning in

decisions which allows for political imperatives. And as we have noted, the Court's 'kid-glove' standard of review (Bernitsas, 1993: 117) has meant that the Court has very rarely been critical of the Commission.

The Court of Justice has consistently upheld the Commission's exercise of its discretionary powers, provided that its decisions meet the essential requirements of Article 190 of the Treaty and that the Commission has been guilty of neither an abuse of power nor of manifest error in reaching its conclusions (Bernitsas, 1993: 117).

It would be misleading however to see the involvement of the College in state aid matters as an entirely separate stage in the decision-taking process. Likewise it would be wrong to assume that it is at this stage alone that the political imperatives become important. Rather, the involvement of the Commissioners' offices can begin early on in the decision-making process and can impact upon the discretionary instances identified in the sections above. This is only the case however when a decision is potentially controversial in one or more member states, and where a difference of opinion is likely to occur amongst the Commissioners.

Inter-service consultations which are a necessary part of the 'contentious' procedure alert the DGs throughout the Commission to a proposal which is likely to be controversial. This information will usually reach the ears of the relevant *cabinet* members who will be alerted early on to a case which is likely to be problematic. They will then try to prepare the ground in advance, taking steps to minimise the likelihood of a clash wherever possible. Informally, soundings-out of fellow *cabinet* officials will give the competition staff a good idea of those Commissioners likely to oppose the DGIV/competition line. It will be clear early on whether opponents have a clear

majority in the College, or whether their opposition is likely to be ineffective (they may in any case be keen industry for domestic political reasons to voice their opposition to a proposal in support of a national industry). Formally, the draft decision will be discussed in a number of forums. The *special chefs* meetings are the meetings of cabinet officials responsible for specific policy areas, one of which is state aid. With most of the preliminary soundings-out done informally, these meetings serve to iron out difficulties whilst confirming the official line of the *cabinets*/Commissioners for the record.

At the chefs de cabinet meeting, the heads of the *cabinets* may also have an opportunity to review the proposed decision, once again confirming the areas of disagreement and reaching a decision that the issue is controversial enough to be discussed in the weekly Commissioners' meeting. The desired image of unity that the College often attempts to project convinces few. Conflicts have been much publicised, particularly in the financial press. On the whole, these conflicts emerge around three poles: around the balance between state interventionism and the free market (ideological differences); around multi-faceted national cleavages (territorial differences); and around internal institutional constraints (functional differences). However, these distinctions are in practice blurred and often indistinguishable. Conflict often appears to focus on national-EU tensions which is perhaps in the nature of the beast given that the law pits the Commission directly against national governments (Bishop 1997: 84). Those governments often put a great deal of pressure on the individual Commissioners to follow the 'national' line.

The process of decision-taking in controversial cases in many ways mirrors decision-taking in the Council of Ministers, with bargaining, log-rolling and consensus-

building part-and-parcel of the way in which decisions are ultimately taken. This is not peculiar to the state aid domain, although it is not surprising that the Commission should seek to recreate itself as a pseudo-Council, given that the Council's involvement in state aid policy is, as we have seen, fairly marginal.

Although attention has focused on the decision-taking role of the College, increasingly decisions ostensibly taken by the College are in fact issued under an accelerated procedure.

In all areas where the Commission's discretionary power is circumscribed by precise assessment criteria which are laid down in notices, guidelines and communications to Member States, decisions on schemes or cases are usually taken by way of delegation or powers, by the Member of the Commission responsible for state aid. Today, this amounts to 45% of all decisions in the field of state aid' (Mederer, 1997).

In such cases it is the College of Commissioners as well as the Council of Ministers which is excluded from the decision-taking process.

State aid policy-making: limiting discretion

Discretion comes in many forms. Conventionally it is the administrative discretion identified above which underpins the distinctiveness of the EU's state aid regime. However, this is only a partial analysis of the Commission's discretionary potential as it is in the Commission's ability to *make policy*, rather than 'simply' to *take decisions*, that the most novel characteristics of the state aid regime are identified. Through the

medium of a wide range of guidelines, criteria and principles,¹⁰ the Commission limits its own administrative discretion whilst paradoxically enhancing its policy (and its political) role by creating a framework by the analysis made in individual decisions is guided. Just as in the case of administrative discretion, there are clear limits to the Commission's policy-making function. It cannot formally legislate of course, and in the majority of cases the Commission will seek the informal approval of member state representatives in multilateral meetings. In addition, the Commission is not only constrained by the threat of judicial review, but also by the treaty framework, and more recently by the burgeoning body of case-law which itself rests upon individual state aid decisions.

Although some commentators are quick to claim the 'absence of an explicit framework or guidelines for the systematic assessment of competition issues' (Bishop, 1997: 84), this is only accurate to the extent that such a framework ought to be judiciable. Arguments about whether Commission guidelines are binding or not continue and dominate much of the legal literature on the state aid guidelines (Rawlinson, 1993; Hancher et al. 1993, 11). However, from a political/administrative perspective it would be wrong to see the state aid regime as anything other than rule-based (Kobia, 1996), although one should not presume from this that the application of the policy is always consistent.¹¹ Indeed, '[n]o one could, for a moment, assume that in an area as highly charged by political and social considerations as state aids policy that one could expect the Commission to apply a rigid, formalistic or mechanistic approach to controlling national state aids' (Hancher et al., 1993: 10). Indeed, the Commission

¹⁰ Frameworks, Notices, Communications, Policy statements in the annual Competition reports, Codes, the DGIV Newsletter and principles such as the market investor principle and the compensatory justification principle (often contained with the guidelines)

¹¹ Faull (1994) would disagree however. He argues that '[t]oday, the Commission has at its disposal a broad set of clear-cut, transparent and consistently applied rules in the field of state aid control'.

has occasionally found itself in trouble with the Court for changing its own rules in what might be perceived to be a rather *ad hoc* manner.¹²

Guidelines emerge as the Commission's state aid policy matures. Rather than creating the policy, the guidelines are merely a concrete expression of criteria which has in the past been applied to a particular sector or type of aid. Guidelines are not just about substantive policy criteria however. They involve the clarification of procedural matters as well as substantive ones (della Cananea, 1993: 63-4). Indeed, on the procedural side there is less case-law (Hancher, 1994: 134) which suggests that the Commission has something of a freer hand in framing the procedural practice of the state aid regime. In this way it is possible to identify over time a gradual formalisation of policy and procedures: the translation of the practice of individual decisions and court judgements into criteria applied (largely) across-the-board; the translation of that criteria into policy statements and guidelines and the constant updating and tightening up of those guidelines; and ultimately (although we are perhaps only early in this stage), the translation of guidelines into law. This process of policy formalisation has characterised the evolution of the EU's state aid regime, though it has rarely followed a smooth and linear path. Indeed, the Commission clearly has to base its practice in the first place on the treaty provisions and on the judgements of the Court and does not have the freedom to extend and alter obligations placed on member states and firms at will (Hancher et al. 1993: 11). Nevertheless, it is clearly the Commission that drives the process, entailing standard-setting and regulation to create an administratively (if

¹² See the ECJ's ruling of 24 March 1993 in Case 313/90, *CIRFS v. Commission*. See Hancher et al. (1993: 10) for details of the case, in which the Court criticised the Commission for interpreting its own guidelines on synthetic fibres in different ways in different cases. The Commission cannot alter the meaning of its guidelines simply by issuing an individual decision as this would not meet the principle of equal treatment and legitimate expectation.

not legally) binding framework within which individual cases are investigated and individual decisions are taken.

This process of policy formalisation comes at a price: the loss of discretionary power (Ehlermann, 1995). As Rawlinson (1993: 55) has stated '[p]olicy frameworks on state aid, like all rules, reduce the Member States' room for manoeuvre in giving aid and the aid controller's margin of discretion, choice and possible arbitrariness'. So why, we might ask, is the Commission party to such an approach? Rawlinson (1993) identifies three motives: first, timesaving, namely the desire for speedy decision-taking and the cutting back of backlogs; second, a commitment to the goals of transparency, legal certainty and the credibility of state aid enforcement mechanisms; and third, the desire for an ever tighter control of aid levels. We might add to that the Commission's desire to use its state aid control powers in a strategic long-term fashion, as means of contributing to the broad treaty objectives of market integration and cohesion. Clearly, the creation of a body of guidelines implies a loss of flexibility on the part of the Commission, but this loss is deemed to be a price worth paying for the advantages gained, especially given that the guidelines are often seen to be more useful as *internal* labour-saving policy tools at the disposal of Commission officials, than as *external* statements of policy (though of course the two may not be mutually exclusive).

Rawlinson (1993: 58) notes that '[t]he Commission needs rules to discipline itself. Rules are the best safeguard against political decisions which, if they were to proliferate, would destroy all state aid control'. The assumption here is that it is discretion which is political, and this 'political' element infers an *ad hoc*ery on the part of the Commission. It is clear however that using a more inclusive definition of politics leads us to different conclusions. Indeed, the Commission's policy-making

process which results in the creation of guidelines is judged here to be a *political* activity. The restriction of discretion, as well as its exercise, is thus political. The creation of guidelines is viewed, therefore, as the 'structuring of discretion' (della Cananea, 1993: 70) rather than the destruction of it.

Conclusion

This paper's examination of the interplay between discretion and criteria tells us that the Commission acts not only as a *decision-maker* but also as a *policy-maker* in the state aid domain. Decision-making, the adoption of individual decisions, involves the exercise of formal enforcement powers. These are none-the-less political in that the Commission is obliged to make use of instances of discretion at its disposal (whether at the level of the official or within the college of commissioners). The executive decision-taking function of the Commission implies that the Commission acts as a 'quasi-legislator'. This function is a conventional one as 'legislation concerning economic and social policy always involves the delegation of discretion to the executive' (della Cananea, 1993: 74).

Somewhat less conventionally, however, the Commission also has a major role to play as the prime state aid *policy-maker*. This function involves the development of broad strategies and criteria for action and the clarification of the means through which those strategies are to be implemented. Although formally it is for the Council of Ministers to agree to implementing decisions (through Article 94) the Commission has *de facto* usurped that role, translating by informal means the Council's legitimate policy-making function into a regulatory responsibility all of its own. This

responsibility has its margins of course and is far from existing in an institutional vacuum. Both the Council, and to a much greater extent the Court (with its case-law) are crucial in determining what does and does not become Commission policy. Nevertheless, Commission policy-making is a highly political function which can be a great deal more controversial than policy initiation. Policy-making on state aid matters clearly has discretion at its core. Without this discretion, there could be no scope for the self-imposed limits placed by the Commission on its own freedom of manoeuvre, and thus for the guidelines and principles which act as the building-blocks of the policy.

But are there broader lessons or insights that we might be drawn from this assessment of state aid policy? It is certainly true that state aid matters operate in a policy and institutional environment very different from other Community competences. The autonomy the Commission has in this policy area, though constrained, is certainly unique. As a result, there must be doubts as to whether generalisations made from the specific state aid case can in any way be meaningful.

Nevertheless, there are three more general conclusions that are drawn from the body of this paper. The first emphasises the importance of discretion as a means of forging a regulatory or policy-making role for the Commission, and stretches our conception of the Commission's functions beyond those conventionally identified (namely, initiation, management, representation, mediation, administration etc.). Such a conventional interpretation of what the Commission does should not constrain our understanding of that institution, for behind what are formally *executive* functions, a more informal and more *political* policy role may be identified.

A second conclusion highlights the importance of the Commission-Court relationship in this same context. It is clear that the law and politics of state aid control are inextricably intertwined. The Court plays a dual role vis-a-vis the Commission here. On the one hand, it serves to demarcate the margins of both its discretionary scope and its policy-making function. On the other hand, it confirms and formalises Commission discretion and policy-making where this is deemed to be in line with treaty objectives and legal precedent.

Finally, there are conclusions to be drawn about the role of politics in the state aid regime and in its analysis. Dominated as it is by legal and, to a lesser extent, by economic analysis, it is ironic that research on one of the most politically controversial of all the EU policies has largely been ignored by political scientists.¹³ This has meant that mainstream discourse about state aid has revolved around issues of legality, legal precedent and the tensions between law and economics. This paper does not in itself seek to readdress this imbalance in the state aid literature. It does, however, assert that a move away from conventional state aid analyses which view politics disparagingly, as something undesirable, would be beneficial. Rather than wishing for a world (or a state aid regime) without politics, we must stop seeing a political state aid regime as incompatible with an effective policy and begin to relish the political dimension of state aid control.

¹³ There are a very limited number of exceptions. See for example Lavdas and Memindrou (1995) who try to address this criticism.

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APPENDIX 1

Directorate G of Directorate-General IV (DGIV) of the European Commission

1. State aid policy
2. Horizontal Aid
3. Regional Aid
4. Steel, non-ferrous metals, mines, shipbuilding, cars, synthetic fibres
5. Textiles, paper, chemicals, pharmaceuticals, electronics, mechanical and other manufacturing industry, construction
6. Public undertakings and services
7. Analysis, inventories and reports

APPENDIX 2

State Aid Provisions of the Treaty (as amended by the TEU)

Aids Granted by States

ARTICLE 92

1. Save as otherwise provided in this treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market.

2. The following shall be compatible with the common market:

(a) aid having a social character, granted to individual consumers, provided that such aid is granted without discrimination related to the origin of the products concerned;

(b) aid to make good the damage caused by natural disasters or exceptional occurrences;

(c) aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany, in so far as such aid is required in order to compensate for the economic disadvantages caused by that division.

3. The following may be considered to be compatible with the common market:

(a) aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment;

(b) aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;

(c) aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest. However, the aids granted to shipbuilding as of 1 January 1957 shall, in so far as they serve only to compensate for the absence of customs protection, be progressively reduced under the same conditions as apply to the elimination of customs duties, subject to the provisions of this Treaty concerning common commercial policy towards third countries;

(d) aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest;

(e) such other categories of aid as may be specified by decision of the Council acting by a qualified majority on a proposal from the Commission;

ARTICLE 93

1. The Commission shall, in co-operation with Member States, keep under constant review all systems of aid existing in those States. It shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the common market.

2. If, after giving notice to the parties concerned to submit their comments, the Commission finds that aid granted by a State or through State resources is not compatible with the common market having regard to Article 92, or that such aid is being misused, it shall decide that the State concerned shall abolish or alter such aid within a period of time to be determined by the Commission.

If the State concerned does not comply with this decision within the prescribed time, the Commission or any other interested state may, in derogation from the provisions of Article 169 and 170, refer the matter to the Court of Justice direct.

On application by a Member State, the Council, may acting unanimously, decide that aid which that State is granting or intends to grant shall be considered to be compatible with the common market, in derogation from the provisions of Article 92 or from the regulations provided for in Article 94, if such a decision is justified by exceptional circumstances. If, as regards the aid in question, the Commission has already initiated the procedure provided for in the first subparagraph of this paragraph, the fact that the State concerned has made its application to the Council shall have the effect of suspending that procedure until the Council has made its attitude known.

If, however, the Council has not made its attitude known within three months of the said application being made, the Commission shall give its decision on the case.

3. The Commission shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. If it considers that any such plan is not compatible with the common market having regard to Article 92, it shall without delay initiate the procedure provided for in paragraph 2. The Member State concerned shall not put its proposed measures into effect until this procedure has resulted in a final decision.

ARTICLE 94

The Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament, may make any appropriate regulations for the application of Articles 92 and 93 and may in particular determine the conditions in which Article 93(3) shall apply and the categories of aid exempted from this procedure.